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No.

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In the Supreme Court of the United States

OCTOBER TERM, 1987

EDWARD J. HALLORAN, APPELLANT

v.

STATE OF NEW YORK, APPELLEE

On Appeal from the Supreme Court of New York, Appellate Division, First Department

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JURISDICTIONAL STATEMENT

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QUESTIONS PRESENTED

1. Whether the Due Process Clause is violated by a New York statute that provides for use of the civil "preponderance of the evidence" standard in a criminal sentencing proceeding in which the maximum sentence authorized by law depends upon a factual determination of the amount of the defendant's "gain" from the crime.

2. Whether appellant's $25,000,000 fine as his "gain" from a misdemeanor, which was based in part on amounts that were untainted by the offense, violated the Eighth and Fourteenth Amendments because it was disproportionate to his offense and in excess of the penalty authorized by law.

3. Whether the state courts' interpretation of the term "gain," which was the basis for appellant's $25,000,000 fine for a misdemeanor, deprived appellant of constitutionally required fair notice because it involved an unforeseeable judicial expansion of a criminal statute.

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JURISDICTIONAL STATEMENT

OPINIONS BELOW

The order denying leave to appeal to the New York Court of Appeals (App., *infra*, 1a) is unreported. The order of the Supreme Court of New York, Appellate Division, First Department, affirming appellant's conviction and sentence (*id.* at 3a) is reported at 521 N.Y.S.2d 962 (1987) (Table). The opinion and order (App., *infra*, 5a) and the oral ruling (*id.* at 10a) of the Supreme Court of New York imposing sentence on appellant are unreported.

JURISDICTION

The order of the Court of Appeals denying leave to appeal was entered on December 15, 1987 (App., *infra*, 1a). An application for reargument or reconsideration of that order, pursuant to N.Y. Ct. of App. R. 500.10(b), was denied on January 25, 1988 (App., *infra*, 2a).

Because the courts below rejected appellant's constitutional challenges to the New York statutes under which

his fine was imposed, an appeal lies to this Court pursuant to 28 U.S.C. § 1257(2). See, *e.g.*, *Ulster County Court* v. *Allen*, 442 U.S. 140, 149 n.7 (1979). A notice of appeal to this Court was filed on March 9, 1988, in the Supreme Court of New York, Appellate Division, First Department (App., *infra*, 23a). Under 28 U.S.C. § 1257(2), this Court has jurisdiction not only over any issue that gives rise to the appeal but also "over any aspects of the case which would otherwise fall solely within our certiorari jurisdiction." *Cox Broadcasting Corp.* v. *Cohn*, 420 U.S. 469, 487 n.14 (1975).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

A. The Due Process Clause of the Fourteenth Amendment provides:

> [N]or shall any State deprive any person of life, liberty, or property, without due process of law * * *.

B. The Eighth Amendment provides:

> Excessive bail shall not be required, nor excessive fines imposed, nor cruel and unusual punishments inflicted.

C. Section 80.05 of the New York Penal Law provides in pertinent part:

> 1. Class A misdemeanor. A sentence to pay a fine for a class A misdemeanor shall be a sentence to pay an amount, fixed by the court, not exceeding one thousand dollars * * *.
>
> * * * * *
>
> 5. Alternative sentence. If a person has gained money or property through the commission of any misdemeanor or violation then upon conviction thereof, the court, in lieu of imposing the fine authorized for the offense under one of the above subdivisions, may sentence the defendant to pay an amount, fixed by the court, not exceeding double the amount of the defendant's gain from the commission

of the offense. In such event the provisions of subdivisions two and three of section 80.00 shall be applicable to the sentence.

D. Section 80.00 of the New York Penal Law provides in pertinent part:

> 2. As used in this section the term "gain" means the amount of money or the value of property derived from the commission of the crime, less the amount of money or the value of property returned to the victim of the crime or seized by or surrendered to lawful authority prior to the time sentence is imposed.
>
> 3. When the court imposes a fine for a felony pursuant to paragraph 2 of subdivision one of this section, the court shall make a finding as to the amount of the defendant's gain from the crime. If the record does not contain sufficient evidence to support such a finding the court may conduct a hearing upon the issue.

E. Section 400.30 of the New York Criminal Procedure Law provides in pertinent part:

> § 400.30 Procedure for determining the amount of a fine based upon the defendant's gain from the offense.
>
> * * * * *
>
> 4. Burden and standard of proof; evidence. At any hearing held pursuant to this section the burden of proof rests upon the people. A finding as to the amount of the defendant's gain from the commission of the offense must be based upon a preponderance of the evidence. Any relevant evidence, not legally privileged, may be received regardless of its admissibility under the exclusionary rules of evidence.

STATEMENT

Section 80.05 of the New York Penal Law provides that, upon conviction for a class A misdemeanor, the defendant may be fined either $1,000 or twice the amount of his gain from the offense. "Gain" is defined (§ 80.00(2))

as "the amount of money * * * derived from the commission of the crime, less the amount of money * * * returned to the victim of the crime * * * prior to the time sentence is imposed." Pursuant to this statute, appellant Edward J. Halloran was fined *$25 million* for a check kiting *misdemeanor* notwithstanding that prior to sentencing he had returned *all* of the money taken from the banks.

To reach this result, the trial court read the term "gain" in an unprecedented and most improbable manner, construing it to mean not only the amount of money that was wrongfully obtained but also any profit or appreciation in the business or property in which the proceeds of the offense had been used. And the court compounded the unfairness of its novel construction by interpreting "gain" to include the entire amount of such profit or appreciation, even though much of it was attributable to investment of funds not even arguably derived from the offense. Finally, in determining the amount of this "gain," the court rejected appellant's argument that the Constitution required it to apply a higher standard of proof than the civil "preponderance of the evidence" standard provided in the statute, thereby basing the penalty on insufficient (and vigorously contested) factual findings.

Despite the staggering amount of the fine imposed on appellant, and despite the serious issues raised concerning the application and validity of the New York statute, the Appellate Division wrote no opinion in affirming the trial court's judgment, and the Court of Appeals denied appellant leave to appeal. Thus, the New York courts left standing appellant's $25 million fine for a misdemeanor without providing any explanation for rejecting his substantial contentions.

A. The Charges And The Trial

In an indictment returned on June 27, 1985, appellant Halloran and co-defendant Harold Madden were charged

with two felony counts of grand larceny in the second degree, in violation of N.Y. Penal Law § 155.35 (McKinney 1975), and one misdemeanor count of scheme to defraud in the second degree, in violation of N.Y. Penal Law § 190.60 (McKinney 1988 Supp.). These charges arose from a "check kite" operated by the defendants between approximately April 1, 1983, and March 30, 1984, involving accounts at Citibank and Marine Midland Bank in New York City. Because no issue is raised here concerning appellant's conviction, the charges and the trial may be briefly summarized.

The prosecution's evidence at trial showed that appellant had various holdings including the Taft Hotel in New York, the Holiday Inn in Fort Washington, Pennsylvania, and several concrete companies. In order to maintain these businesses and pay outstanding obligations, appellant sought additional bank loans but was largely unsuccessful in securing them. He thereupon turned to the check kiting scheme to obtain the necessary funds.

The defendants conceded that they had operated the check kite. They also acknowledged that the year-long kite entailed thousands of checks with face amounts totaling billions of dollars (primarily reflecting the ever-escalating nature of a check kite, which is necessary to avoid detection). And they admitted that there was a $23 million shortfall in the account at Marine Midland Bank after Citibank discovered and terminated the kite. Thus, there was no dispute that the defendants had engaged in an extensive check kite involving large sums of money.

The jury acquitted both defendants on the larceny counts but convicted them on the misdemeanor fraud count. With respect to the larceny charges, the defense presented to the jury was that defendants had not intended permanently to deprive the banks of the kited funds, which is an essential element of larceny. The

evidence showed that appellant had adequate assets at all times to cover the amount of the kite, that he always intended to make good the checks when sufficient cash became available, and that he sought to generate funds to reduce or end the kite.

Immediately after discovery of the check kite, appellant entered into an agreement and novation with Marine Midland Bank in full settlement of all amounts owed to the bank. This agreement encompassed the $23 million deficiency from the kite as well as nearly $3 million in existing loans to appellant and his father. In addition to repayment of these amounts, the agreement provided for interest at a specified rate plus various fees and expenses. Tr. 2005-2016; A.D. App. A7.[1] Appellant fully paid off the amount due Marine Midland Bank in September 1984, following his sale of several properties (Tr. 2019-2021; A.D. App. A34-A36).

B. The Sentencing Hearing And The $25 Million Fine

1. Section 80.05(1) of the New York Penal Law provides a maximum fine of $1,000 for a misdemeanor such as the scheme to defraud of which appellant was convicted. It also authorizes an "[a]lternative sentence" if the defendant "has gained money or property through the commission" of the offense. In that circumstance, the court "may sentence the defendant to pay an amount, fixed by the court, not exceeding double the amount of the defendant's gain from the commission of the offense." Section 80.05(5) incorporates by reference the definition of "gain" set forth in section 80.00(2):

> As used in this section the term "gain" means the amount of money or the value of property derived from the commission of the crime, less the amount of money or the value of property returned to the victim of the crime or seized by or surrendered to

[1] "A.D. App." refers to appellant's appendix in the Appellate Division.

lawful authority prior to the time sentence is imposed.

In imposing an alternative sentence, the court is required to "make a finding as to the amount of the defendant's gain from the crime." N.Y. Penal Law 80.00(3). If that finding cannot be made on the existing record, the court "may conduct a hearing upon the issue." *Ibid.* At this hearing, relevant and non-privileged evidence "may be received regardless of its admissibility under the exclusionary rules of evidence." N.Y. Crim. Proc. Law § 400.30(4). Of immediate significance here, Section 400.30(4) expressly provides that the burden of proof at the hearing, while resting on the prosecution, is merely a "preponderance of the evidence."

2. Pursuant to these statutory provisions, the trial court conducted a hearing to determine the amount of defendants' gain. The prosecution conceded that *all* of the $23 million check kiting deficiency (plus an additional $2.9 million) had been repaid to the banks. Nevertheless, it sought a fine in excess of $50 million based on the theory that defendants had a "gain" of more than $25 million, consisting of (a) the interest they saved that would have been incurred if the $23 million in funds had been obtained through loans (alleged to be $2.3 million), and (b) the appreciation alleged to have occurred in three of appellant's businesses or properties in which the proceeds of the kite had been used—the Holiday Inn ($1.65 million), the concrete companies ($6.1 million), and the Taft Hotel ($17.1 million). A.D. App. A69-A76. The prosecution relied almost entirely on net worth evidence that had been introduced by appellant during the trial to show, in defense against the felony counts, his ability to repay in full moneys obtained during the kite.

Appellant presented the testimony of his accountant. That testimony demonstrated that appellant's profit from the Taft Hotel during the period of the check kite was far less than indicated by the source relied on by the

prosecution—the capital gain reported for federal income tax purposes. For example, appellant incurred $12 million in operating losses on the Taft Hotel during the time the capital gain alleged by the prosecution was accruing, leaving him with an actual net gain only a tiny fraction of that shown by the capital gains schedule, yet the prosecution's calculation did not adjust his "profit" from the hotel by that amount. Tr. 361, 446, 1849, 1851, 1882, 1886; A.D. App. A490. Similarly, the prosecution claimed as "gain" appreciation in book value of the concrete companies and the Holiday Inn that was attributable to investment of funds derived from the kite, even though the kite proceeds had been fully repaid.

3. On this record, the trial court concluded that appellant's "gain" was "in excess of $22,000,000.00" (App., *infra*, 22a).[2] Although it specifically declined to "impose a fine of double the gain" (*ibid.*), the court, without further explanation, sentenced appellant to a fine of $25 million.[3]

The trial court levied this enormous fine despite its recognition that the banks had been made whole by appellant's repayment of the entire kite deficiency, and despite the statutory provision that "gain" means "the amount of money * * * derived from the commission of

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[2] The court reduced the prosecution's figure for gain from the Taft Hotel by the expenses incurred in its sale. App., *infra*, 15a, 17a.

[3] Appellant was also sentenced to a term of six months' imprisonment.

Appellant objected in the trial court that the sentencing proceeding and the amount of the fine violated the Due Process Clause and the Eighth Amendment. See A.D. App. A82-A83, A100. Likewise, appellant's brief in the Appellate Division argued (at 52, 75, 83-93) that the statute violated the Due Process Clause because it applied the "preponderance of the evidence" standard and did not give fair notice of the meaning of the term "gain" as interpreted by the trial court, and also that it violated the Eighth Amendment insofar as it authorized the $25 million fine.

the offense, less the amount of money * * * returned to the victim of the crime." In so doing, the court conceded "that there is no quarrel that there [have] been no fines of this nature ever ordered before" (App., *infra*, 12a), and it candidly acknowledged that the issue of gain "is really rather a difficult one" (*id.* at 14a).

The trial court's determination of "gain" consisted of two elements, interest and appreciation. With respect to unpaid interest, the court cursorily noted that "I see no particular reason why that cannot be considered as a gain to the defendant from this crime" (App., *infra*, 13a). Accordingly, the court concluded, "as requested by the People, that the amount of the gain attributable to the interest not being paid between April 1 of 1983 and March 29, 1984" was $2.3 million (*id.* at 14a-15a).

With respect to the issue of appreciation, the trial court included in appellant's "gain" the entire increase in the value of the Holiday Inn and the concrete companies (App., *infra*, 15a-16a). The court gave no recognition to the undisputed fact that the entire amount of this increased value was due, dollar-for-dollar, to the infusion of kited funds into those businesses, so that any "gain" from such appreciation was completely eliminated by the repayment of the kite deficiency. Instead, the court simply stated that "[i]t seems fair" to treat the best measure of gain as "the increase in net realizable worth" (*id.* at 16a).[4]

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[4] The trial court subsequently "amplif[ied]" its oral ruling that the applicable measure of gain was how much appellant's "businesses appreciated during the course of the fraud" (App., *infra*, 5a, 7a). In the court's view, "it hardly requires financial sophistication to see" that appellant's profits "would inevitably have [been] reduced" if he had sold off some of his assets or secured funds from other investors rather than engaging in the check kite (*id.* at 7a). Thus, "if 'kite' money was put into a business, then obviously its appreciation could be said to be 'derived from the commission of the crime' within the meaning of [Section] 80.00(2)" (*id.* at 8a).

Likewise, the trial court used the full capital gain reported from the sale of the Taft Hotel (App., *infra*, 15a). The court "decline[d]," without explaining why, "to deduct the operating losses of the Taft Hotel" from the gain (*ibid.*). Nor did it take account of appellant's ownership interest in the Taft Hotel prior to the inception of the check kiting scheme or attempt to find the actual pre-kite market value of the hotel, though evidence was introduced showing it to be well in excess of the price Halloran had paid to purchase it. See note 8, *infra*.

Pursuant to N.Y. Crim. Pro. Law § 400.30(4), the trial court reached these fact findings by reviewing the record under the "preponderance of the evidence" standard. Indeed, the court seems to have taken an even more relaxed view of the prosecution's obligation: although the statute places the burden of proof on the government, the court remarked that "when a criminal enterprise has been proved it really should not be up to the prosecution to figure out what the gain is" (App., *infra*, 17a).

4. Notwithstanding the magnitude of the fine imposed for appellant's misdemeanor, and notwithstanding the substantial legal issues presented by the surprising and unprecedented interpretation of the alternative fine statute, the Appellate Division summarily affirmed without opinion (App., *infra*, 3a), and the Court of Appeals denied appellant leave to appeal (*id.* at 1a).

THE QUESTIONS ARE SUBSTANTIAL

Several facts stand out in this appeal. Most strikingly, appellant Halloran, a non-violent first offender, was fined $25 million for a check kiting misdemeanor. Moreover, this fine was imposed even though appellant had repaid the full amount obtained from the kite prior to sentencing, and—as the trial court recognized—the banks had suffered *no* loss from the kite.

In arriving at its sentence, and without pointing to any support in the statute or judicial precedents, the trial

court construed the term "gain" in the New York penal code to extend beyond the commonly understood concept of direct proceeds from the crime to encompass consequential profits or appreciation in the business or property in which the unlawfully obtained money was subsequent used. What is more, the court included all such profits or appreciation in the punishable "gain" without regard to whether any of the increase in value was due to untainted funds of the defendant. These drastic consequences were visited upon appellant on the basis of questionable findings of "gain" that, under the governing New York statute, needed to satisfy only the civil "preponderance of the evidence" standard.

The New York system of alternative criminal fines is unconstitutional both on its face and as applied here. First, the statutory "preponderance" standard violates due process. Because the maximum allowable fine has not been legislatively fixed but depends upon a post-conviction factual determination of "gain," the defendant has a constitutionally protected property interest in not being subjected to criminal punishment of the basis of findings arrived at by application of the lax "preponderance" standard, under which the defendant and the prosecution share an equal risk of factual error. This case well illustrates how the "preponderance" standard permits courts to resolve controverted issues of fact on a basis that is inadequate to sustain serious criminal sanctions.

Second, the courts below applied the New York statute to authorize a fine based on "gain" that includes amounts *not* attributable to a defendant's tainted funds. Such a fine violates the Eighth and Fourteenth Amendments, because, by reaching amounts not reasonably measured by the defendant's illegal "gain," it is disproportionate to his offense and in excess of the punishment authorized by law. Here, for example, appellant was required to pay a fine of $25 million even though, at the time of sentencing, he had derived little or no profit from the check kiting scheme.

Finally, the New York statute did not give constitutionally required fair warning of the state courts' expansive interpretation of the term "gain." No reasonable person viewing the provision for alternative fines would have been aware that the statutorily authorized fine extended to profits or appreciation in the property in which unlawfully obtained funds were used. Moreover, this lack of adequate notice resulted in actual prejudice to appellant in his defense in this case.

The significance of these issues extends well beyond this case. New York's alternative fine statute is based on Section 6.03 of the Model Penal Code (1962),[5] and 15 states in addition to New York have adopted a similar provision.[6] See also, *e.g.*, 18 U.S.C. § 1963(a) and 21 U.S.C. § 855 (alternative fines of "not more than twice the gross profits or other proceeds"). Thus, constitutional questions concerning the applicable standard of proof and the permissible limits of the term "gain" are both important and recurring. Likewise, courts are divided over the standard of proof and the extent of the forfeitable interest under the analogous forfeiture provisions in the federal Drug Control Act, 21 U.S.C. §§ 848

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[5] Section 6.03 provides:

> A person who has been convicted of an offense may be sentenced to pay a fine not exceeding:
>
> * * * * *
>
> (5) any higher amount equal to double the pecuniary gain derived from the offense by the offender * * *.

[6] See Ala. Code § 13A-5-11 (1982); Alaska Stat. § 12.55.035 (1984); Ark. Stat. Ann. § 5-4-201(d) (1987); Conn. Gen. Stat. Ann. § 53a-44 (West 1985); Del. Code Ann. tit. 11, § 4208(6) (1987); Fla. Stat. Ann. 775.083 (West 1987); Haw. Rev. Stat. § 706-640 (1985); Ky. Rev. Stat. Ann. § 534.030 (Michie/Bobbs-Merrill 1985); Me. Rev. Stat. Ann. tit. 17A, § 1301(1)(D) (1983); Mo. Ann. Stat. § 560.016 (Vernon 1979); N.H. Rev. Stat. Ann. § 651:2 (IV)(c) (1986); N.J. Stat. Ann. § 2C:43-3(e) (West 1982); Or. Rev. Stat. § 161.635 (1985); 18 Pa. Cons. Stat. Ann. § 1101(7) (Purdon 1983); Wash. Rev. Code Ann. § 9A.20.030(1) (1987).

and 853, and the Racketeer Influenced and Corrupt Organizations Act (RICO), 18 U.S.C. § 1963(a). A decision in this appeal would furnish needed clarification on these significant constitutional issues.

Taken individually, each of appellant's challenges to his unprecedented and ruinous $25 million fine demonstrates a constitutional violation that warrants this Court's review. Taken together, they compellingly depict a sentencing process run amok that—in view of the stony indifference of the state appellate courts—only this Court can correct. Because the questions presented by this appeal are substantial, and because a summary dismissal would bind all courts confronting these issues in the future, probable jurisdiction should be noted.

I. THE NEW YORK STATUTE VIOLATES THE DUE PROCESS CLAUSE BY APPLYING THE "PREPONDERANCE OF THE EVIDENCE" STANDARD TO FACT FINDINGS THAT DETERMINE THE MAXIMUM CRIMINAL PENALTY AUTHORIZED BY LAW

This case presents an important issue left unresolved by the Court's recent decision in *McMillan* v. *Pennsylvania*, 106 S.Ct. 2411 (1986): whether the Due Process Clause requires that a standard of proof higher than the "preponderance of the evidence" be applied in making factual determinations that serve to establish the maximum criminal penalty that is authorized by law.

A. Criminal statutes typically provide a maximum penalty, prescribed by the legislature, to which a defendant is subject. Under such a statute, the defendant, once having been convicted, may be sentenced in the discretion of the court to any punishment within the statutory range. While the sentencing proceeding must, of course, be fundamentally fair,[7] the convicted defendant does not

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[7] See, *e.g.*, *Zant* v. *Stephens*, 462 U.S. 862, 887 n.23, 903 (1983); *Gardner* v. *Florida*, 430 U.S. 349, 358 (1977) (plurality opinion); *Townsend* v. *Burke*, 334 U.S. 736, 740-741 (1948); *Roberts* v. *United States*, 445 U.S. 552, 563 (1980) (Brennan, J., concurring).

have a liberty or property interest that is implicated by the level of the authorized penalty that the court chooses, and there is no set of facts he could prove that would entitle him to one sentence rather than another. It was for this reason that the Court explained in *McMillan* that "[o]nce the reasonable doubt standard has been applied to obtain a valid conviction, 'the criminal defendant has been constitutionally deprived of his liberty to the extent that the State may confine him' " (106 S.Ct. at 2420 n.8; citation omitted). See also *Vitek* v. *Jones*, 445 U.S. 480, 491-494 (1980).

The present case is fundamentally different. Under the New York statutory structure, the fact of conviction does *not* subject the defendant to a deprivation of property beyond the $1,000 fine specified by the legislature. Instead, a greater fine may be imposed only upon proof of the amount of the defendant's "gain" from the crime, which is determined at a second judicial proceeding. Thus, the factual determination of "gain" fixes the maximum penalty that is authorized by law; a finding of a larger "gain" increases the severity of the available punishment.

The Court's analysis in *McMillan* reflects the critical distinctions between these two situations. The Court there upheld, 5-4, a Pennsylvania statute that prescribed a "preponderance" standard for determining whether a defendant "visibly possessed a firearm" and therefore was subject to a mandatory minimum sentence. In sustaining the "preponderance" standard, the Court emphasized that the Pennsylvania law did not affect the maximum allowable sentence but instead merely limited the trial court's discretion to impose a lesser penalty (see 106 S.Ct. at 2414, 2417-2418, 2419). Because the statutory factor did not enhance the maximum penalty, defendants sentenced under the firearms provision were subject to no greater punishment—and had no greater due process

rights—than under a traditional criminal statute, and the Court "s[aw] no way to distinguish the visible possession finding at issue here from a host of other express or implied findings sentencing judges typically make on the way to passing sentence" (*id.* at 2420 n.8).

The Court recognized, however, that a different question would be presented "if a finding of visible possession exposed [defendants] to greater or additional punishment" (106 S. Ct. at 2418). The Court was willing to accept arguendo that the "preponderance" standard would be unconstitutional in a case like *Specht* v. *Patterson*, 386 U.S. 605 (1967), where the defendant was subject to an enhanced penalty if found to be dangerous at a post-verdict hearing, but it distinguished *Specht* as involving " 'a radically different situation' from the usual sentencing proceeding" (106 S. Ct. at 2418, quoting 386 U.S. at 608). This case presents that "radically different situation," and the Court should now decide whether the "preponderance" standard is constitutionally tolerable in such a circumstance.

B. Because an increase in the maximum allowable penalty based on a post-conviction factual determination implicates substantial constitutionally-protected interests of the defendant, the Due Process Clause requires that such a determination be made by a standard of proof more stringent than the civil "preponderance of the evidence" standard prescribed in the New York statute.

The constitutional choice of a standard of proof reflects the level of reliability that is appropriate to a given fact-finding. "The standard serves to allocate the risk of error between the litigants and to indicate the relative importance attached to the ultimate decision." *Addington* v. *Texas*, 441 U.S. 418, 423 (1979). In this way it " 'instruct[s] the factfinder concerning the degree of confidence our society thinks he should have in the correctness of factual conclusions for a particular type of adjudication' " (*ibid.*, quoting *In re Winship*, 397 U.S. 358, 370

(1970) (Harlan, J., concurring)). "Increasing the burden of proof is one way to impress the factfinder with the importance of the decision and thereby perhaps to reduce the chances that inappropriate [determinations] will be [made]" (441 U.S. at 427).

The "preponderance" standard is constitutionally insufficient for the factfinding required by the New York alternative fine statute. Under the "preponderance" standard, "[t]he litigants * * * share the risk of error in roughly equal fashion" (*Addington*, 441 U.S. at 423). "Use of that standard reflects the judgment that society is nearly neutral between erroneous" decisions in favor of one party or the other (*Santosky* v. *Kramer*, 455 U.S. 745, 765 (1982)) and thus "has a minimal concern with the outcome" (*Addington*, 441 U.S. at 423). Where what is at stake is a matter as serious as the maximum criminal punishment that may lawfully be inflicted, however, society is not neutral on the question of who should bear the risk of error.

Sentencing involves, first of all, an adversarial criminal proceeding between the individual and the state. And, in contrast to civil proceedings, a criminal sentence is by its nature punitive, and the defendant cannot fairly be made to bear the predominant risk that an unduly severe maximum penalty will be set as the result of an erroneous factual determination. Moreover, an enhanced maximum penalty increases the defendant's stigma: the greater punishment is an indication of the degree of condemnation that society attaches to the offense.

This Court has consistently required at least "clear and convincing evidence" in other situations in which, as here, "particularly important individual interests or rights are at stake." *Herman & MacLean* v. *Huddleston*, 459 U.S. 375, 389 (1983). Such a heightened standard is simply an expression of the constitutionally mandated "preference for one side's interests" (*id.* at 390); "[i]n cases involving individual rights, * * * '[t]he standard

of proof * * * reflects the value society places on individual liberty'" (*Addington*, 441 U.S. at 425 (citation omitted)). In this case, as in cases like *Addington* (441 U.S. at 427) and *Santosky* (455 U.S. at 768), "[t]he individual should not be asked to share equally with society the risk of error when the possible injury to the individual is significantly greater than possible harm to the state."

In addition, unlike in *McMillan*, the choice of the proper standard is of great practical importance to the accurate determination of the statutory enhancement factor. This Court noted in *McMillan*, as the Pennsylvania Supreme Court had explained, that "the risk of error in the context of [the statutory sentencing] proceeding is comparatively slight—visible possession [of a firearm] is a simple, straightforward issue susceptible of objective proof" (106 S.Ct. at 2415). Under the New York statute as construed in this case, by contrast, the finding of "gain" involves potentially complex factual inquiries tracing the investment history of criminal proceeds and entails a meaningful risk of error.

C. In the instant case, it is most unlikely that the determination of appellant's "gain" would have been the same if a standard higher than "preponderance of the evidence" had been applicable. The prosecution relied on excerpts from the trial record to support its contentions regarding gain, although the amount of the gain from appellant's investment of kite proceeds was at most a peripheral issue during the trial. On the other hand, appellant introduced testimony by his accountant at the sentencing hearing that focused specifically on that critical issue. The trial court brushed aside this testimony—which completely contradicted the prosecution's evidence—suggesting that it might have been given greater weight if appellant had proffered the evidence from some other source (App., *infra*, 8a). Surely the court could

not have treated the fact-finding process so cavalierly if the prosecution had been held to a stricter burden of proof.

The determination of "gain" on the Taft Hotel provides the clearest illustration of the importance of the standard of proof in this case. The trial court measured appellant's "gain" from the offense by the amount his properties increased in value during the period of the kite. To compute that figure (assuming that it represents the legally correct test of "gain"), the court first had to determine the value of the Taft Hotel prior to the kite. Only by finding what the Taft Hotel was worth at that point could the court calculate the increase in its value as the "gain" from the kite.

The trial court, however, made no finding of the pre-kite value of the Taft Hotel. Rather, it used the capital gain on the sale of the hotel that appellant reported for income tax purposes as the measure of the appreciation of the hotel during the time of the kite. But substantial doubt was cast on the reliability of that figure by evidence showing that appellant had acquired the Taft Hotel prior to the kite for a purchase price that was nearly $8 million below market value.[8] Thus, while the actual purchase price was the correct basis for tax purposes, a trier of fact could readily have found that its use artificially inflated the apparent increase in value of the Taft Hotel within the kite period by almost $8 million. Moreover, since appellant ultimately sold the Taft Hotel (and other properties) at distress prices in order to repay the kite deficiency (*e.g.*, Tr. 2000-2001, 2128-2129), and since

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[8] The evidence established that appellant had acquired full ownership of the Taft Hotel in early February 1983 (two months before commencement of the kite) for $20 million. At that time the hotel was appraised at $27.8 million (of which $17 million was attributed to the land alone). In fact, as early as 1981, appellant and his then-partner had rejected an offer of $27.6 million for the hotel. Tr. 413-414, 446, 1706, 1851, 1896.

he had incurred operating losses of $12 million on the hotel during the period he was supposedly accruing a $14.2 million gain (see page 8, *supra*), the court's uncritical acceptance of the tax return figure as the basis for its finding is most questionable.

If the evidence adduced by appellant at the sentencing hearing with regard to the Taft Hotel had been accepted, the largest component of gain found by the trial court would have disappeared. Similar problems accompanied other facets of the gain findings. See page 8, *supra*. Plainly, then, the selection of a standard of proof was vitally important to determining the amount of the fine that could be imposed. The sentencing court almost certainly could not have reached its flimsy findings under a standard requiring "clear and convincing evidence," much less proof "beyond a reasonable doubt."

D. The courts of appeals are divided over an analogous standard-of-proof issue that arises under the federal RICO and drug forfeiture statutes (18 U.S.C. § 1963; 21 U.S.C. §§ 848 and 853). In *United States* v. *Horak*, 833 F.2d 1235, 1243 (7th Cir. 1987), the court recognized that "the government must prove the relevant facts beyond a reasonable doubt to win forfeiture under section 1963 [of RICO]." Similarly, in *United States* v. *McKeithen*, 822 F.2d 310, 312 (2d Cir. 1987), the court noted that "[t]he government * * * carries the burden of proof beyond a reasonable doubt" for criminal forfeiture under the drug statute. By contrast, the Third Circuit has upheld the "preponderance of the evidence as the government's burden of proof for criminal forfeiture after a guilty verdict" in a drug prosecution. See *United States* v. *Sandini*, 816 F.2d 869, 870, 874-876 (3d Cir. 1987), disapproved in *Horak*, 833 F.2d at 1243. This disarray regarding the governing standard of proof demonstrates the substantial nature of the question presented in this appeal and the need for this Court's review.

II. APPELLANT'S FINE IS EXCESSIVE BECAUSE IT FAR EXCEEDS HIS "GAIN" FROM THE OFFENSE AND TAKES INTO ACCOUNT PROFITS UNRELATED TO THE OFFENSE

We take it as indisputable that a $25 million fine for a misdemeanor would be unconstitutional in the absence of some special justification. In this case, the asserted justification was that appellant "gained" that amount from his offense. As noted above, the trial court assessed that "gain" by including all of the appreciation that the court believed had occurred during the course of the offense in three properties in which the kited funds were used—the Taft Hotel, the Holiday Inn, and the concrete companies. The fine also reflected appellant's "gain" due to "saved interest." See page 9, *supra*.

This fine was unconstitutional in two respects. First, the statute as construed authorized a fine that was excessive and disproportionate, in violation of the Eighth Amendment, because its amount was not measured solely by appellant's profit from the offense but also reflected appreciation on his properties that was wholly unrelated to any tainted funds. Second, even accepting the validity of the construction given to the fine statute, the fine exceeded the penalty authorized by the statute because the trial court engaged in substantial double counting of "gain" and included amounts of "gain" that appellant never in fact realized.

A. At the core of the Eighth Amendment is the concept of proportionality. As the Court explained in *Solem* v. *Helm*, 463 U.S. 277, 284, 286 (1983), "[t]he principle that a punishment should be proportionate to the crime is deeply rooted," and "[t]he constitutional principle of proportionality has been recognized explicitly in this Court for almost a century." Thus, the Eighth Amendment requires that "a criminal sentence must be proportionate to the crime for which the defendant has been convicted" (*id.* at 290). Appellant's fine violated this

principle because it was based in substantial part on profits not derived from his criminal offense.

The clearest example of this defect is the trial court's treatment of the Taft Hotel. The court applied the New York statute to impose a fine that included the *entire* appreciation on the hotel during appellant's ownership, not just the portion attributable to the investment of kited funds. This led to an excessive and disproportionate penalty for two reasons. First, the court ignored the fact that appellant acquired the Taft Hotel prior to the kite, and thus some of the appreciation could have had nothing to do with the kite. See page 18 & n.8, *supra*. Second, even if all of the appreciation in the hotel had occurred within the kite period, not all of it derived from appellant's use of the kited funds. Rather, at most, the appreciation was allocable to both the kited funds and appellant's untainted and far larger pre-kite $20 million investment in the hotel.

In effect, the trial court determined appellant's "gain" from the kite as if he had misappropriated the money to acquire the hotel in the first place and then sold it at a profit; but that of course is not what happened. The difference between the two situations demonstrates that the court's theory of "gain" completely disregarded the appreciation attributable to appellant's legitimate investment. The Eighth Amendment, however, does not permit the State to divest appellant of untainted income in the guise of criminal "gain," any more than it would permit the imposition of a fine in the amount of twice the defendant's profits from all of his investments in the stock market simply because he had purchased some stock with misdemeanor proceeds.

Several courts have recognized that the Eighth Amendment strictly limits the forfeiture of a defendant's property to that attributable to his criminal conduct. In *United States* v. *Busher*, 817 F.2d 1409, 1415 (9th Cir. 1987), for example, the court of appeals held that the

forfeiture of the defendant's entire interest in a legitimate business used as a RICO enterprise would violate the Eighth Amendment if the interest forfeited is disproportionate to "the degree to which the enterprise operated by the defendant is infected by criminal conduct." The court applied the same Eighth Amendment principle to the drug forfeiture statute in *United States* v. *Littlefield*, 821 F.2d 1365 (9th Cir. 1987). Likewise, in *United States* v. *Walsh*, 700 F.2d 846, 857 (2d Cir.), cert. denied, 464 U.S. 825 (1983), the court of appeals noted that the Eighth Amendment would prohibit forfeiture of a defendant's entire interest in a RICO enterprise that is substantially engaged in a legitimate business. See also *United States* v. *Horak*, 833 F.2d 1235, 1251 (7th Cir. 1987) (citing with approval the Eighth Amendment analysis in *Busher*, *Littlefield*, and *Walsh*).[9]

Under the principles embraced by these decisions, appellant's $25 million fine violates the Eighth Amendment. At the same time, other courts have construed the Eighth Amendment to allow forfeitures that are not proportionate to the defendant's offense. See, *e.g.*, *United States* v. *Grande*, 620 F.2d 1026, 1039 (4th Cir.), cert. denied, 449 U.S. 830 (1980), which the court in *Busher* expressly declined to follow (817 F.2d at 1414-1415 n.9).

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[9] See also *United States* v. *McKeithen*, 822 F.2d at 315 (the drug forfeiture statute is confined to the "proportional forfeiture" of property tainted by an offense; such forfeiture is "consistent with the legislative aims of deterrence, and destruction of economic power bases, of criminal profiteers," but the government's position seeking full forfeiture could lead to "bizarre" results and "would appear to [have] no limiting principle"); *United States* v. *Zang*, 703 F.2d 1186, 1195 (10th Cir. 1982), cert. denied, 464 U.S. 828 (1983) (the interest acquired by the use of racketeering funds is subject to forfeiture under RICO, but "untained interests" are not forfeitable and "should be protected").

A case involving a similar issue of proportionality under the Excessive Fines Clause of the Eighth Amendment is currently awaiting decision by this Court. *Bankers Life & Cas. Co.* v. *Crenshaw*, No. 85-1765 (argued Nov. 30, 1987).

This divergence over the restrictions imposed by the Eighth Amendment on criminal penalties is an important and recurring issue that warrants the Court's review in this case.

B. The trial court's finding of "gain" exceeded appellant's actual "gain" in another respect as well: it was based on substantial amounts of purported "gain" that either were double counted or did not constitute a benefit to appellant. Because the New York alternative fine statute provides a maximum penalty that is a function of the defendant's "gain," an erroneous determination of "gain" results in the judicial imposition of punishment beyond that authorized by law. Such a fine is an elementary violation of due process, which "prohibit[s] state courts from depriving persons of liberty or property as punishment for criminal conduct except to the extent authorized by state law." *Whalen* v. *United States*, 445 U.S. 684, 690 n.4 (1980).

One instance of impermissible double counting arises from the trial court's treatment of "saved interest" and appreciation. In essence, appellant's crime was to take by fraud a substantial loan that he could not obtain by legitimate means. Under the prosecution's interpretation of the fine statute, it was arguable that appellant's "gain" included not just the principal amount of this "loan" but also the interest he saved by obtaining money through commission of the offense. Once that interest was accounted for, however, the court should not also have included in appellant's "gain" the appreciation in his properties in which the kited money had been invested. The amount of "saved interest" represented a return on the use of the kited funds. There was no basis for attributing two returns—interest and appreciation—to those funds.

The trial court also grossly overstated appellant's profit from the offense by counting as "gain" the increase in book value of the Holiday Inn and the concrete com-

panies. The undisputed evidence at the sentencing hearing showed that those properties experienced no intrinsic appreciation during the kite period and that any increase in their value was due entirely to the investment of the kited funds. See page 9, *supra*. Because appellant had repaid the kite deficiency in full, it was improper double counting to include in appellant's "gain" the apparent appreciation on the Holiday Inn and the concrete companies that in fact represented money he had previously returned.

Finally, in calculating the punishable "gain" on the Taft Hotel, the trial court refused to deduct the $12 million in operating losses that appellant incurred while allegedly accumulating his "gain." See page 8, *supra*. By so doing, the court attributed to appellant a "gain"—the total appreciation on the Taft Hotel—that in fact he never had. Even under the court's theory that the check kiting scheme enabled appellant to retain the Taft Hotel, his benefit would consist of the *net* amount by which he was enriched by retaining the hotel during the period of the kite, and a fine measured by that amount would be rationally related to his illegal profits. The court's artificial separation of the asserted "gain" on the Taft Hotel from the losses incurred in its retention credited appellant with a nonexistent "gain" and resulted in a fine that exceeded the maximum penalty authorized by law.

III. THE NEW YORK STATUTE FAILED TO GIVE CONSTITUTIONALLY REQUIRED FAIR NOTICE OF THE STATE COURTS' EXPANSIVE INTERPRETATION OF THE TERM "GAIN"

In requiring appellant to pay a $25 million fine, the trial court embraced an unforeseeable and virtually limitless interpretation of "gain" to include all profits or appreciation on appellant's property in which the kited funds were used. This after-the-fact judicial expansion of a criminal statute violated due process by depriving appellant of fair warning of the punishment provided for his offense. What is more, the lack of notice lulled ap-

pellant into a trap that prejudiced his defense and, in particular, allowed the prosecution to turn his trial testimony against him at the sentencing hearing. In an adversarial system of criminal justice, a statute that fails fairly to announce its meaning cannot be permitted to be used as a self-incriminatory snare for the unwary.

A. Because it is a "fundamental tenet of due process that '[n]o one may be required at peril of life, liberty or property to speculate as to the meaning of penal statutes,' " a criminal statute is invalid if it " 'fails to give a person of ordinary intelligence fair notice' " of what it provides. *United States* v. *Batchelder*, 442 U.S. 114, 123 (1979) (citations omitted). This principle is fully applicable to "vague sentencing provisions" that "do not state with sufficient clarity the consequences of violating a given criminal statute" (*ibid.*).

As this Court has consistently recognized, "[t]here can be no doubt that a deprivation of the right of fair warning can result * * * from an unforeseeable and retroactive judicial expansion" of a criminal statute. *Bouie* v. *City of Columbia*, 378 U.S. 347, 352 (1964); see also *Rabe* v. *Washington*, 405 U.S. 313 (1972) (per curiam); *Douglas* v. *Buder*, 412 U.S. 430 (1973) (per curiam); *Marks* v. *United States*, 430 U.S. 188, 191-195 (1977). The due process vice is "precisely like [that in] an *ex post facto* law" (*Bouie*, 378 U.S. at 353), which " 'imposes a punishment for an act which was not punishable at the time it was committed * * * or imposes additional punishment to that then prescribed.' " *Weaver* v. *Graham*, 450 U.S. 24, 28 (1981) (citation omitted); see also *Marks*, 430 U.S. at 191-192.

The trial court's unprecedented and unnatural interpretation of the statutory term "gain" failed to satisfy the due process requirement of fair notice. The "alternative fine" statute had been on the books for 20 years at the time appellant was sentenced. 1965 N.Y. Laws, ch. 1030 (effective Sept. 1, 1967). During that period, many in-

dividual and corporate defendants were convicted of pecuniary crimes associated with their business activities. If the prosecution's interpretation of the statute were correct, or even plausible, many fines should have been imposed (or at least proposed by other prosecutors) based on calculation of profits or appreciation subsequently accruing from any property in which illegally obtained funds were invested, and there should have been a substantial proliferation of judicial opinions explicating the principles that would guide such highly speculative inquiries. Instead, as the trial court frankly conceded, "no fines of this nature [have] ever [been] ordered before" (App., *infra*, 12a).

In fact, the statute belies the trial court's reading. Section 80.00(2) of the N.Y. Penal Law provides in plain and unambiguous language that "gain" is "the amount of money or the value of property derived from the commission of the crime." Moreover, like the alternative fine provisions adopted in five other states,[10] Section 80.00(2) expressly provides an offset from the defendant's "gain" for "the amount of money or the value of property returned to the victim of the crime or seized by or surrendered to lawful authority prior to the time sentence is imposed." Reading these two clauses together, the statute clearly indicates that the defendant's "gain" from the crime is to be based on the amount of money or the value of property that was unlawfully obtained from, and not returned to, the victim of the crime. The evident purpose of this section is to make the victim whole and to deter the defendant from attempting to retain any of the victim's money or property; it is not to penalize the defendant out of all proportion to the victim's loss.

The failure of Section 80.00(2) to afford fair notice of the trial court's sweeping interpretation is also shown by a comparison of that statute and the forfeiture provisions of New York law. Article 13-A of the N.Y. Civil

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[10] See the statutes of Alabama, Arkansas, Maine, Missouri, and Oregon cited in note 6, *supra*.

Practice Law and Rules provides a post-conviction civil action for the forfeiture of the "proceeds of a crime." This phrase is expressly defined to mean "any property obtained through the commission of a felony crime * * *, *and includes any appreciation in value of such property*" (N.Y. Civ. Prac. L. & R. § 1310(2) (McKinney 1988 Supp.) (emphasis added)) or the "substituted proceeds of a crime"—which is "any property obtained by the sale or exchange of proceeds of a crime, *and any gain realized by such sale or exchange*" (*id.* at § 1310(3) (emphasis added)). In addition, N.Y. Penal Law § 460.30 (McKinney 1988 Supp.) provides a criminal forfeiture penalty for the racketeering offense of "enterprise corruption"; this forfeiture extends to "any interest, including proceeds," that the defendant has "acquired or maintained in an enterprise" or "*derived from an investment*" of unlawfully obtained funds (*id.* § 460.30(1)(b,c) (emphasis added)). These forfeiture provisions, which expressly refer to appreciation and proceeds from investment or sale, refute the trial court's blithe assumption that Section 80.00(2) was designed *sub silentio* to incorporate the same principles.

Moreover, these forfeiture provisions are circumscribed by substantial procedural protections. For example, the criminal enterprise statute provides for a jury determination of the forfeiture issue, requires "proof beyond a reasonable doubt" based on "relevant and legally admissible evidence," and permits mitigation of the forfeiture if the jury or the court finds it is "disproportionate" to the defendant's "gain" or "conduct" (§ 460.30(1)(a,b,c), 2(b,c)). The absence of similar safeguards from the summary hearing under the alternative fine statute strongly suggests that the general term "gain" in Section 80.00(2) could not reasonably have been understood to require resolution of complex issues of appreciation.

B. The lack of adequate notice not only denied appellant fair warning of the penalty for his offense but sub-

stantially prejudiced him in defending against the prosecution's effort to impose a mammoth fine. Appellant's defense to the felony larceny counts was to prove that he did not intend permanently to deprive the banks of the kited funds and that at all times he possessed the capacity to make full repayment. Because counsel understandably believed that appellant, having repaid the kite deficiency, retained no "gain" and therefore was not subject to the alternative fine statute, the defense simply showed appellant's net worth without limiting its evidence to the untainted value of his assets or taking into account any issue of appreciation.[11]

As a result, the prosecution, under its surprise theory of "gain," was able to use appellant's trial evidence against him at sentencing. Indeed, that evidence was the prosecution's *only* proof of the asserted appreciation in the value of appellant's properties. And the trial court was particularly influenced by appellant's own trial evidence in deciding to impose the massive $25 million fine (App., *infra*, 6a-8a).

There can be no doubt that appellant's defense would have been presented differently if he had been given notice of the potential exposure to a multi-million dollar fine under the appreciation theory of "gain." The record shows that appellant had no need to prove any appreciation in his holdings in order to establish his ability to cover the kite deficiency; proof of the unappreciated value of his assets at the beginning of the kite would have been ample. Furthermore, to the extent questions regarding appreciation had arisen at the trial, care would have been taken to be both more circumspect and more precise with respect to a matter that was not in fact

[11] Indeed, had counsel appreciated the risk of financial disaster latent in the alternative fine provision, it is quite likely that appellant would have been advised to seek a plea bargain, even at the expense of pleading guilty to felony counts to which he had a strong defense.

perceived to be relevant. For example, pains would have been taken to bring out the extent to which appreciation of the Taft Hotel occurred prior to the kite and was not attributable in any way to the scheme to defraud. In that event, the trial court would not have been able to rely, as it in fact did (App., *infra*, 8a), on what it perceived to be an inconsistency between appellant's trial and sentencing positions.

In sum, the New York statute failed to give fair warning of the maximum penalty provided by law. The silence of the statute also enabled the prosecution to spring its appreciation theory on an unprepared defendant and convert the shield of appellant's trial defense into a sentencing sword. As a result, appellant's due process rights were seriously prejudiced in this case.

CONCLUSION

Probable jurisdiction should be noted.

Respectfully submitted.

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MARCH 1988

APPENDICES

APPENDIX A

STATE OF NEW YORK
COURT OF APPEALS

Before: HON. FRITZ W. ALEXANDER, II, Associate Judge

THE PEOPLE OF THE STATE OF NEW YORK
Respondent,

against

EDWARD J. HALLORAN,
Appellant.

CERTIFICATE DENYING LEAVE

I, FRITZ W. ALEXANDER, II, Associate Judge of the Court of Appeals of the State of New York, do hereby certify that, upon application timely made by the above-named appellant for a certificate pursuant to CPL 460.20 and upon the record and proceedings herein,* there is no question of law presented which ought to be reviewed by the Court of Appeals and permission to appeal is hereby denied, and the related application for stay of execution is accordingly dismissed.

Dated at New York, New York December 15, 1987.

/s/ Fritz W. Alexander
Associate Judge

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* Description of Order: Order of the Appellate Division, First Department, entered on December 3, 1987, affirming the judgment of the Supreme Court, New York County, rendered on October 31, 1986.

APPENDIX B

STATE OF NEW YORK
COURT OF APPEALS

Before: HON. FRITZ W. ALEXANDER, II, Associate Judge

THE PEOPLE OF THE STATE OF NEW YORK,
Respondent,

—against—

EDWARD J. HALLORAN,
Appellant.

CERTIFICATE DENYING RECONSIDERATION

I, FRITZ W. ALEXANDER, II, Associate Judge of the Court of Appeals of the State of New York, do hereby certify that, upon application for reconsideration timely made by the above-named appellant for a certificate pursuant to CPL 460.20 and upon the record and proceedings for reconsideration herein,* there is no question of law presented which ought to be reviewed by the Court of Appeals and permission for reconsideration is hereby denied.

Dated at New York, New York January 25, 1988

/s/ Fritz W. Alexander
Associate Judge

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* Description of Order: Order of the Appellate Division, First Department, entered on December 3, 1987, affirming the judgment of the Supreme Court, New York County, rendered on October 31, 1986.

APPENDIX C

At a term of the Appellate Division of the Supreme Court held in and for the First Judicial Department in the County of New York, on December 3, 1987

Present—HON. FRANCIS T. MURPHY, Presiding Justice
JOHN CARRO
ERNEST H. ROSENBERGER
BETTY WEINBERG ELLERIN
GEORGE BUNDY SMITH, Justices.

31340

THE PEOPLE OF THE STATE OF NEW YORK,
Respondent,

—against—

EDWARD J. HALLORAN,
Defendant-Appellant.

ORDER OF AFFIRMANCE ON APPEAL FROM JUDGMENT

An appeal having been taken to this Court by the defendant-appellant from the judgment of the Supreme Court. New York County (Carol Berkman, J.), rendered on October 31, 1986, and said appeal having been argued by Frederick P. Hafetz, Lawrence S. Goldman, Roger Parloff and Jeremy Gutman of counsel for the appellant, and by Brian Rosner and Mark Dwyer of counsel for the respondent; and due deliberation having been had thereon,

It is unanimously ordered and adjudged that the judgment so appealed from be and the same is hereby, in all things, affirmed. The case is remitted to the Supreme Court, New York County, for further proceedings pursuant to CPL 460.50(5).

ENTER:

HAROLD J. REYNOLDS
Clerk.

Counsel for appellant is referred to
§ 606.5, Rules of the Appellate
Division, First Department.

APPENDIX D

TRIAL COURT'S WRITTEN OPINION AND ORDER REGARDING SENTENCE

(Pages A-693 to A-695)

SUPREME COURT OF THE STATE OF NEW YORK
NEW YORK COUNTY: PART 66

3955/85

THE PEOPLE OF THE STATE OF NEW YORK,
Plaintiffs

—against—

EDWARD J. HALLORAN and HAROLD F. MADDEN,
Defendants

OPINION AND ORDER

BERKMAN, J.

The defendants have been convicted after a trial by jury of a scheme to defraud in the second degree (CPL 190.60), a class A misdemeanor, and sentenced on October 31, 1986: Edward J. Halloran to a jail term of six months and a fine of twenty-five million dollars ($25,000,000); Harold F. Madden to a conditional discharge with the conditions that he perform one-hundred-twenty (120) hours of community service and pay a fine of one-hundred thousand dollars ($100,000).

This opinion and order is filed to amplify the court's findings with respect to the fines and in compliance with CPL 420.10(6).

Penal Law 80.05(5) provides that "[i]f a person has gained money or property through the commission of a misdemeanor . . . then upon conviction, the court . . . may sentence the defendant to pay an amount, fixed by the court, not exceeding double the amount of the defendant's gain from the commission of the offense." Gain is defined by PL 80.00(2) as "the value of property derived from the commission of the crime, less the amount of money . . . returned to the victim . . . prior to the time sentence is imposed." Penal Law 80.00(3) authorizes a hearing "[i]f the record does not contain sufficient evidence to support . . . a finding of the amount of the gain."

Much of the trial, particularly the defense case, was spent proving what was done with the money obtained through the scheme to defraud and the extent and nature of defendant Halloran's vast wealth. At the sentencing hearing, the People offered witnesses to establish a fair rate of interest for the money obtained through the fraud, which defendant Halloran testified was a mere unauthorized (and thus presumably interest-free) borrowing. The People also offered certain admissions by defendant Halloran, through his attorney, made prior to the institution of this prosecution and with an eye to fending off indictment. These admissions related to Halloran's vast wealth.

Both defendants' testimony at trial made clear that during the course of the scheme to defraud, defendant Halloran and the businesses owned or controlled by him were in a desperate cash-flow position. For example, the Taft Hotel, obtained in February 1983, just before the provable beginning of the check-kiting scheme, suffered multi-million dollar operating losses and needed extensive renovations. (Indeed, it was the defendants' posture at the sentencing hearing that the operating losses should be deducted from Halloran's capital gain on the sale of the Taft.) Additionally, one of the hotels constituting the

so-called Southern Properties, a Holiday Inn, was in imminent danger of losing its franchise unless substantial capital improvements were made. The Concrete Companies were not generating the cash they should because of substantial delinquent receivables.

Defendant Halloran claimed that he sought further credit, but loans were not forthcoming. Notwithstanding Halloran's insistence that he was good for the money, it is apparent that his properties were already too encumbered and not sufficiently profitable to constitute desirable collateral. Halloran did not address the issue of whether he even thought of selling off some of his properties for immediate cash or of seeking investors; but it hardly requires financial sophistication to see that either of those alternatives would inevitably have reduced Halloran's profits.

The defendants' testimony at trial unquestionably established that the funds obtained through the scheme to defraud were the life-blood of Halloran's businesses. Defendant Halloran argued at the sentencing hearing that it is speculative to contend that without the check-kite, Halloran's losses would have been staggering. The defense argued that other salvations would have been possible. It is Halloran's arguments which are speculative. What actually happened, as defendants' proof at trial showed, is that Halloran saved his financial empire by an extensive and elaborate check-kite, in the course of which he took twenty-three million dollars.

The problem before that court at sentencing was measuring this gain. Understandably, rather than undertake to prove what Halloran (and derivatively Madden) would have lost but for their crime, the People showed how much some—far from all—of Halloran's businesses appreciated during the course of the fraud, and how much interest was saved by defendants' fraudulent "borrowings." In choosing the businesses whose appreciation was

shown at the sentencing hearing, the People selected those into which "kite" money had been pumped; if "kite" money was put into a business, then obviously its appreciation could be said to be "derived from the commission of the crime" within the meaning of PL 80.00(2).

At trial, to avoid a grand larceny conviction, the defendants were eager to show the health of Halloran's financial empire. With the jury's discharge, however, the empire became moribund: its gains limited to the amount pumped in from the kite; its losses oppressive and all but wiping out any capital gains. Had the defendants chosen to offer some evidence of this at the sentencing hearing other than the conclusions and opinions of Halloran's accountant, the court would have considered it. But in view of what the defendants' proof established at trial, these self-serving arguments and conclusions at sentence did not rebut the People's evidence that defendants' gains went well beyond the monies taken in the course of the kite and returned to Marine Midland Bank upon discovery of the fraud. The record establishes, without evidentiary contradiction, that the appreciation in the Taft, the Southern Properties and the Concrete Companies was a gain to the defendants within the meaning of PL 80.00(2).

Accordingly, the court found, as set forth in the minutes of October 31, 1986, that the defendants' gain, as defined by PL 80.00(2), was well in excess of twenty-million dollars.

IT IS ORDERED, that defendant Halloran pay a fine in the amount of twenty-five million dollars ($25,000,000) and a mandatory surcharge in the amount of sixty dollars ($60); and

IT IS FURTHER ORDERED, that defendant Madden pay a fine in the amount of one-hundred thousand thousand dollars ($100,000) and a mandatory surcharge in the amount of sixty dollars ($60); and

IT IS FURTHER ORDERED, that the People institute proceedings to collect the fine imposed.

The clerk of the court is directed to serve a copy of this opinion and order on the parties, through their attornies.

The foregoing constitutes the opinion and order of this court.

/s/ Carol Berkman
CAROL BERKMAN
J.S.C.

Dated: New York, New York
November 10, 1986

APPENDIX E

TRANSCRIPT OF SENTENCING HEARING AND SENTENCING OF OCTOBER 31, 1986
(Pages A-418 to A-663)

SUPREME COURT OF THE STATE OF NEW YORK
COUNTY OF NEW YORK: PART 66

Ind. #3955/85

THE PEOPLE OF THE STATE OF NEW YORK,

—against—

EDWARD HALLORAN and HAROLD MADDEN,
Defendants.

Charge: Scheme To Defraud, etc.

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100 Centre Street,
New York, New York,

October 31st, 1986,
A.M. & P.M. SESSION.

HEARING CONTINUED, DECISION
AND SENTENCE

Before:

HON. CAROL BERKMAN, Justice.

Appearances:

ROBERT MORGENTHAU, ESQ.,
District Attorney
New York County,

By: BRIAN ROSNER, ESQ.,
Assistant District Attorney, of Counsel,
For the People.

GOLDMAN & HAFETZ, ESQ.,

By: FREDERICK HAFETZ, ESQ.,
For the Defendant Halloran.

WEIL, GOTSHAL & MANGES, ESQS.,

By: JOHN WING, ESQ., of Counsel,
For Deft. Madden.

ALSO PRESENT:

ROGER PARLOFF, ESQ.

* * * * *

THE COURT: I will say a few things about the issue that I find after a restitution proceeding here.

I have severe doubts, as I have indicated in my colloquy with Mr. Rosner, as to whether or not the sort of restitution sought by the People in this case is contemplated by the section under which the People are proceeding.

I am aware, of course, that if I rule against the People in this regard they have no appeal and that that is final.

On the other hand, neither of the two victims in this matter are helpless. The amounts are substantial and I have some question with regard to what the losses were in view of the operation of the banking system about

which I heard so much, and under all of those circumstances I decline to order any further restitution.

I don't want that to be read as either a statement that the statute does not permit it definitely although I have this problem which I have indicated, or anything more than I have just stated.

With regard to the issue of the fines, I take it that there is no quarrel that there has been no fines of this nature ever ordered before, whether they have been sought before I have not been asked.

I have not heard any argument in that regard and I will assume that to be the case for the moment, although there always has to be a first time and, Mr. Rosner, if you have any prior instances I am sure the Appellate Division would love to hear about them.

That is as to number one, that is 1-A, appearing on Page 2 of the defense memorandum.

As to number 1-B, which refers to CPLR 13A, and Article 460 of the CPL, both of those provisions of the law specifically and explicitly preserve all other remedies and refer explicitly to the finding power of the Court.

I refer to CPLR Section 1352, the presentation of other rights and remedies, and the reference in Article 460 which I need not find specifically at this time to the possibility of fines under Article 80 of the Penal Law.

With regard to whether or not the issues were tried to the jury, or not tried to the jury, I have already dealt with the restitution problem and need not deal with that further. That is under Number 2.

The law is perfectly clear under cases which the defense does not refer to that in a sentencing procedure there is no right to a jury trial. I am not entirely sure there is a separate right to confront the witnesses against one and certainly the summary proceeding has been ap-

proved in a number of instances with regard to the sentencing question.

I will refer to Speziano against Florida, that is recorded at 468 U.S.

I don't have the page citation, 104 Supreme Court, 3154 for 1984 decision, and a more recent decision also of the Supreme Court Macmillian against Pennsylvania, 477 U.S., page cite is not yet available, and that is at 91 Legal Edition, 67.

Of course the cases therein cited, frankly, if one can do without a jury trial when the issue is live I think that that takes care quite clearly of the issue of whether it needs to be a jury trial on the issue of fines.

With regard to whether or not a large fine in this case would be a violation of the Eighth Amendment and of the analogies of the New York State Constitutional provision, I would note, of course, that while this is a misdemeanor, this is an unusually large misdemeanor.

As to that circumstance, it would appear that a large fine would not be out of proportion to the crime committed.

With regard to the issue of interest, at least with regard to the interest being saved, I see no particular reason why that cannot be considered as a gain to the defendant from this crime.

I had, of course, a great deal of evidence at trial with regard to the lack of availability of lending sources, the expense of those lending sources which were available and, indeed, I recall very specifically and very vividly Mr. Halloran saying:

"They should have lent me the money. I was good for it."

I recall that quite vividly.

With regard to findings of gain, it would appear to be reasonable, I should note that obviously the issue of gain or what the gain is whether it is interest or anything else is really rather a difficult one.

I am not sure, indeed, that the Article 80 contemplates even so specific in detail the hearing as we have had in this case.

Obviously, for example, taking the rate of interest that Citibank or Marine Midland charges on their Citibank Plus Account, on their—I don't recall the name of the other account—there is a choice and I suppose in some sense it is an arbitrary choice.

Mr. Halloran seems to think that he is entitled to be charged only prime rate interest.

I really don't know all that much about it. I have not sought too many loans myself and I suspect I could not get one at prime rate, but Mr. Halloran has many more assets than I do, so perhaps he would have that advantage.

However, I have to pick some number which is a reasonable number as a rate of interest in this regard and it appears to me that while the rate of interest which has been referred to in the course of this hearing has to do with a different sort of an account, and it has to do with the real overdrafts as opposed to overdrafts that nobody knows about, or overdrafts that do not really exist because of the operation of the banking system, it is unsecured types of loan at the will of the customer.

Therefore, it appears fairly close and adjusts to the situation that we have here in this case.

I will, accordingly, find as requested by the People, that the amount of the gain attributable to the interest not paid between April 1 of 1983 and March 29, 1984 is one billion six hundred ninety-three thousand dollars—

excuse me and one dollar, that the interest on that amount to September 30, 1986 from April 1 of 1984 is three hundred seventeen thousand four hundred thirty-eight dollars, that the interest on the amounts from Marine Midland from April 1, 1983 to March 29, 1984, that gain was $317,876.68.

I decline to deduct the operating losses of the Taft Hotel gained by the sale of the Taft.

I understand, of course, that for Federal income tax purposes all the gains and losses go into one pot, although not exactly at the same rate in order to come up with the bottom line of taxable income.

However, that I believe would be a rather strange way of calculating the gain in this case and, accordingly, I find the gain with regard to the sale of the Taft Hotel to be $14,186,718.00.

With regard to the Southern properties and the concrete companies, I am not an accountant but I do recall the testimony at trial with regard to the problems that Mr. Halloran was facing in keeping his business going.

He told us at that time that one of the problems was that the Southern hotels which we are dealing with now was in bad shape and in danger of losing its franchise.

I inferred from that and Mr. Acox (phonetic) to some extent confirmed that day explicitly that the loss of a franchise could have rather serious effects upon the vitality of that hotel.

I don't know exactly what the effects might be, I have no specific evidence that I recall before me with respect to whether or not—well, excuse me—I do.

I believe Mr. Halloran referred to the fact that if he lost his franchise he might have some problem with his lenders who, of course, were lending on that assumption.

As to whether or not that hotel would have gone into bankruptcy or not that, of course, is something on which we, of course, can only speculate because Mr. Halloran did not allow that to happen.

With regard to the concrete companies, much the same can be said.

It is, of course, unfortunate and one cannot condone the fact that the customers were not paying their bills which was part of the problems that were going on here.

I suppose that what might have happened and, of course, I don't know because this was not permitted to happen, is what happened to many businesses when their customers were not paying their bills, to wit, that the company goes into the red and possibly into bankruptcy eventually, depending on how bad the situation might be.

All of this, of course, is only speculative.

I cannot say or could not expect it to be said, certainly by proof beyond a reasonable doubt, that these things would have happened.

It is perfectly clear overall from Mr. Halloran's testimony that had he not taken rather extreme measures as he did, that he would have lost a great deal of money. I don't know how much.

It seems fair, therefore, to conclude that the best available nonspeculative measure he gave is the increase in net realizable worth.

Accordingly, I am finding the gain with regard to the Southern properties in the amount of one million four hundred sixty-one thousand six—four hundred sixty-one thousand sixty-one dollars and with regard to the concrete companies a gain of $6,119,780.00.

Against this gain, and this is—this already has been offset by the amounts returned to Marine Midland, it must also be offsetting the amount seized by Citibank.

There is no evidence that that is before me. I think I can safely find that that is in the approximate amount of $585,000.00.

I understand, of course, that there were a number of expenses that Mr. Halloran incurred during the course of this enterprise. Mr. Halloran, I believe, you referred to them in the course of your statement to the Court.

Now, I don't agree with the People and I believe they have—I am not sure they meant to, but to some degree they stated from their position that the expenses of the sale should not be subtracted from the gain on the Taft Hotel.

It seems to me that the ordinary and legitimate expenses of the sale of an asset of this sort are obviously something to be offset against the sale price to come up with what the gain is.

On the other hand, a number of other things which you mentioned, Mr. Hafetz, do not seem to me to be in the same category and those are particularly and most obviously penalties, legal fees assessed by Marine Midland, special fees for taking out loans as Mr. Halloran testified to which would seem to me to be really quite a part from this.

I believe that the import of the decision, I believe it is gross, that the People relied upon in their memorandum is really essentially that when a criminal enterprise has been proved it really should not be up to the prosecution to figure out exactly what the gain is, much less the operating expenses of the enterprise.

And also short of a more realistic statement by the defense, it would seem to be that it is fair to me to simply to ignore that sort of expense as an offset against the gain.

With regard to the nature of this offense and what has been said in the course of the sentencing, I frankly do not

know, perhaps a misread Mr. Rosner but I didn't at any time during this trial think that he had a purpose to describe sentencing against the rich and in some way to bring them to a proceeding before a Court simply by reason of their wallet.

The crime in this case is a crime which requires that you be rich in the first instance.

Were Mr. Halloran or his entities not rich in the first instance he would not have had accounts which permitted the manipulation involved in this case, nor would the banks have so easily overlooked this manipulation.

This is, after all, a con game and all con games whether they are handkerchief switches or extended check kites require to some degree on the breed of the victim, and the banks were happy having these large accounts there and were, therefore, perhaps not as careful as they should have been and as they have now become in watching what was happening as the handkerchief got switched or the shells got moved around, or whichever con game you might prefer to use as an analogy.

Nor did I have any impression whatever that the jury responded by discriminating against the rich.

To the contrary, the jury's acquittal of the defendants on the Grand Jury charge would indicate fully that the jury was prepared to accept the defense which was proffered by the defendants and that is, indeed, a defense of the rich.

It was perfectly obvious during the course of not only the defense case but of the People's entire case that we heard about Mr. Halloran's immense wealth.

So to criticize Mr. Rosner for referring to a law for the rich really does somewhat misstate the nature of the defense here.

I have no particular aversion for the rich. I really would rather be rich myself but I am not, and that is

all right, and I really do not think that the record should be left with any indication that that has played any part either in the verdict in this case, which it really did not, other than the acquittal on the felony charge or in the Court's sentencing.

The fact is that this is a crime of the rich.

With regard to the larceny charges, I frankly found a number of things about the issues presented in the course of the trial leaving aside the questions presented to me on his inspection of the Grand Jury to be very troublesome and to be very difficult.

I believe that the jury did as well, and that had to do with the intent to repay, what the meaning was of the intent to repay.

Frankly, I think that a jury's conclusion that an intent to repay, but that funds were such—in such danger that that was irrelevant would have been absolutely sustainable on the evidence in this case, particularly if the jury heard some of the evidence that has been offered by the defense today.

I think it would have been sustainable but, on the other hand, I have no disagreement with the conclusion that the jury did reach. It was a very troublesome type of issue and I believe the jury did, indeed, give the benefit to the defendants, the benefit of the doubt which they were instructed to do.

On the other issue, the issue of the misrepresentation, I think this case more than any other that I have handled illustrates for me the reason for the rules which say that you have to give the People basically the benefit of the doubt on the inspection of the Grand Jury Minutes because I believe that the issue charged is somewhat from the inspection of the Grand Jury Minutes in my understanding this indictment on the Grand Jury Minutes, and what I heard at trial, particularly after the defendant testified.

The flushing out of what happened here and how it happened, and how the defendants did it, and what their intent was when they did it, I think makes this case really extremely different from the Williams situation, and may very well bring into play, I think it was a footnote in Williams which talked about banking understanding and whether there was evidence as to what that might or might not be.

In any event, it would seem to me that the evidence at this trial presents the issue which I dealt with on the Grand Jury Minutes in a very, very different light and one far more favorable to the prosecution than they bear, essentially, in the Grand Jury presentation and that bears both on the Grand Jury presentation.

I am aware, of course, that neither defendant has a prior record and I'm aware, of course, that there were not a great many cases, and so forth which talk about white collar crimes and what should or should not be done in terms of sentencing people to jail when there is need for room in the jails.

The people who commit violent crimes, and that is all very well but I have a problem with regard to Mr. Madden—excuse me, Mr. Halloran.

I will start with Mr. Halloran because Mr. Halloran, it is perfectly obvious from his testimony and all the evidence that I heard before me at this trial, was the guiding light of this enterprise. He did not do much, more of the work.

Mr. Madden did a lot of the work, Mr. Palitzi did some of the work, but he ordered it done and it was done.

The king of this empire was Mr. Halloran and when he testified at trial and said that he was ashamed, I didn't believe him. Whether the jury did or not I don't know, but I didn't believe him.

What I believed is what he said when he said they should have lent him the money, "I was good for it." I believe that he believes that now and whether he will always believe it or not, I don't know.

All I know is that most of us when we go to a bank and ask for a loan and they turn us down, we have to think of alternative forces of action. We have to sell some of our assets or we have to do without, and Mr. Halloran was not willing to do that, not at all.

He instructed and it was done and I am sure that from all that I have seen was the way he is used to things happening.

I would tend to agree with the People that the maximum sentence here is a year, and I am aware, however, as I said Mr. Halloran has no prior record and I am aware that for a man like him a jail sentence would be particularly difficult.

I am also aware in a case of this nature that any sentence that I have to give is one that will have more deterrent effect than usual because usually when I impose a sentence nobody knows about it except the defendant who receives it, and, indeed, to judge by the press I never impose a jail sentence at all for anything and the state prison and the city prison have become full by neither I nor any of my colleagues having made them full by some process of osmosis because everyone gets slaps on the wrists and returns to the street instantly.

So the deterrent effect of the normal sentence in this courthouse is probably not so great at least on other people. I don't know what it is on at least the defendant being sentenced.

That is not the situation here.

With regard to Mr. Halloran he is sentenced to a term of six months and I am going to impose, I will not impose a fine of double the gain, I take it that the double

gain provision was inserted because of the difficulty of proving what the gain has actually been, or at least that is one of the major reasons, and that the legislature wants to be sure that there were no profits left from the crime.

The gain, as I add it up, in the excess of $22,000,000.00 and I am imposing a fine on Mr. Halloran of $25,000,000.00.

There is an addition, a mandatory surcharge of $60.00.

With regard to Mr. Madden, I find this much more troublesome.

I don't entertain the notion that being appointed to the bench makes me capable of being a spiritual advisor, and I gather from the evidence at the trial that Mr. Madden has people who are more suited to be spiritual advisors than I am.

* * * *

APPENDIX F

IN THE SUPREME COURT OF NEW YORK,
APPELLATE DIVISION, FIRST DEPARTMENT

New York County Indictment No. 3955/85

THE PEOPLE OF THE STATE OF NEW YORK
Respondent,

—against—

EDWARD J. HALLORAN,
Defendant-Appellant.

NOTICE OF APPEAL TO THE
SUPREME COURT OF THE UNITED STATES

Notice is hereby given that appellant Edward J. Halloran appeals to the Supreme Court of the United States from the final order of the Supreme Court of New York, Appellate Division, First Department, entered December 3, 1987, affirming the judgment of conviction in this case.

This appeal is taken pursuant to 28 U.S.C. § 1257(2).

/s/ Jeremy Gutman
Counsel for Appellant
GOLDMAN & HAFETZ
60 East 42nd Street
New York, New York 10165
(212) 682-7000

Dated: March 9, 1988